UNITED STATES BANKRUPTCY COURT EASTERN DISTRICT OF WISCONSIN

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AUDREY L. DANIELS,

Case No. 94-20144

Debtor.

Chapter 13

AUDREY L. DANIELS,

Plaintiff,

V.

Adv. No. 11-2150

COLLECTION TECHNOLOGY, INC., CTI,

Defendant.

MEMORANDUM DECISION ON DEFENDANT'S MOTION TO DISMISS

The plaintiff, Audrey L. Daniels, filed this adversary proceeding against the defendant, Collection Technology, Inc., CTI (hereinafter "CTI"), to enjoin the latter's collection efforts of an allegedly discharged student loan, for return of the garnished wages, and for sanctions for the alleged violation of the discharge injunction. The defendant filed a motion to dismiss for failure to state a cause of action upon which relief may be granted.

This is a core proceeding under 28 U.S.C. § 157(b)(2)(A), (B) and (O), and the Court has jurisdiction under 28 U.S.C. § 1334. The following constitutes the Court's findings of facts and conclusions of law pursuant to Fed. R. Bankr. P. 7052. For the reasons stated below, the defendant's motion is denied.

BACKGROUND

In the early-1980s, the debtor obtained student loans¹ to attend the University of Wisconsin - Milwaukee. The debtor filed a chapter 13 petition on January 11, 1994, and the University of Wisconsin Board of Regents in Milwaukee received notice of the case. Ms. Daniels' Plan provided the following:

Debtor will pay \$25.00 bi-weekly for a period of 36 months by income assignment [via a wage order with the debtor's employer, Milwaukee Public Schools]. Payments to be increased to \$50.00 bi-weekly in 12 months. Student loans to be paid a sum certain before any payments to the unsecured creditors. Mercury Finance to be paid outside the plan. Unsecured creditor to be paid 5% of their allowed claims. Trustee shall pay Attorney for debtor \$1000 as attorney fees.

(Plan of Arrangement filed January 11, 1994).

On May 7, 1991, the University had obtained judgment against the debtor in the amount of \$4,566.64. Garnishments may have taken place in 1992 and 1993, the results of which are not part of the record. By the time of her bankruptcy, apparently the debtor still disputed the amount owed, and at some point during the proceedings, the dispute was resolved. The agreement was reflected in the confirmation order, which included this additional provision: "Mercury Finance paid directly by Debtor. UW of Wis paid \$1000.00." (Order Confirming Plan dated May 24, 1994). The confirmation order was subsequently modified and provided, in relevant part:

The debtor will increase her bi-weekly payment to the Trustee by making payments of \$80.00 bi-weekly for the balance of the plan. No payments to be made during the months school [the debtor's employer] is not in session. Student loan to UWM to be paid \$1000.00 in full settlement of its allowed claim. Student loan to Great Lakes to be in full as filed. Mercury Finance claim, as filed, to be paid in full settlement

¹The amounts and nature of the student loans are unclear from the record. The debtor scheduled the University's claim in the amount of \$4,800, as disputed. The 1991 judgment was entered for \$4,566.64. The debtor also had separate loans with Great Lakes Higher Education Corporation.

of all claims against the debtor and co-debtor and said payment will now be inside the plan. Unsecured creditors to be paid 5% of their allowable claims after claim of Mercury Finance and allowed claims for student loans, as allowed, are paid in full. All other provisions of the original confirmed plan shall not be modified.

(Order Modifying Confirmed Plan of Arrangement dated May 23, 1995).

The University did not file a proof of claim and was not paid through the plan. The debtor completed the plan and received a discharge on April 30, 1999. On or about January 20, 2010, the assignee and/or collection agent for the University, CTI, notified the debtor that it was acting on behalf of the U.S. Department of Education to collect a debt arising from a student loan. Somehow, apparently without further garnishment proceedings in state court, on or about May 1, 2010, CTI contacted the debtor's employer, and garnishment of the debtor's wages took place. As of the filing date of the adversary proceeding, CTI had collected \$3,834.00.

ARGUMENTS

The parties disagree on the arrangement reached between the debtor and the University pre-confirmation regarding how the amount of UWM's claim, agreed to be \$1,000, was to be paid, as well as on the interpretation and effect of the plan provisions. They have not raised the effect of the relevant bankruptcy code provisions applicable to the debtor's 1994 case.

The debtor alleges that CTI failed to take adequate precautions to ensure the accuracy of its communications with her employer as to its right to collect from the debtor's wages. Its unwarranted and procedurally defective collection actions created an undue hardship for the debtor. The debtor's position is that because the University never filed a proof of claim in the underlying chapter 13 case, the plan completed without payment, and the obligation was discharged. CTI's resulting violation of the discharge injunction is thus, according to the debtor,

sanctionable under 11 U.S.C. § 105(a). The debtor also seeks return of the garnished wages.

CTI moved to dismiss the complaint, arguing the debtor failed to set forth any cognizable causes of action. CTI did not willfully disregard the chapter 13 discharge order because it did not act with the knowledge that the University's debt had been discharged. The plan provided that student loans were to be paid separately before other unsecured claims. According to CTI, the debtor and the University agreed the latter's reduced claim would be paid directly from the debtor, outside the plan. This intent was clumsily documented in the first confirmation order, which stated, "Mercury Finance paid directly by Debtor. UW of Wis paid \$1000.00." The University, therefore, deliberately did not file a proof of claim. The decision to not file a claim is supported by the second confirmation order, which provided: "Student loan to UWM to be paid \$1000.00 in full settlement of *its allowed claim*. Student loan to Great Lakes to be in full *as filed*." Again, although awkwardly drafted, the confirmation order presumes the agreement of the parties: the settled claim of the University was deemed allowed in the amount of \$1,000, and it was to be paid directly by the debtor outside the plan, in contrast to the other student loan creditor, Great Lakes, which filed a proof of claim and was paid through the plan.

DISCUSSION

When considering a defendant's Rule 12(b)(6) motion to dismiss, a court shall construe the complaint in the light most favorable to the plaintiff, accepting as true all well-pleaded facts and drawing all possible inferences in its favor. *Cole v. Milwaukee Area Technical College Dist.*, 634 F.3d 901, 903 (7th Cir. 2011). Dismissal is appropriate if the complaint fails to include sufficient facts "to state a claim for relief that is plausible on its face." *Justice v. Town of Cicero*, 577 F.3d 768, 771 (7th Cir. 2009) (quoting *Ashcroft v. Iqbal*, 129 S.Ct. 1937, 1949)

(2009)).

The defendant has moved to dismiss Counts I and III because they are duplicates and fail to state a cause of action. These counts are similar in that the complaint alleges after the defendant was informed by the plaintiff that the debt was discharged, and the plaintiff knowingly provided inaccurate information to the debtor's employer to induce the employer to transmit money the defendant had no right to. The complaint alleges bad faith and willful conduct on the part of the defendant that resulted in an abuse of the bankruptcy process. While conveying inaccurate information is not a cognizable tort, knowingly using inaccurate information to induce another to pay over money that belongs to someone else, especially without state court action which would have allowed her due process to challenge the action, sounds in fraud. Taken as a whole, the complaint plausibly alleges that the defendant knowingly used inaccurate information to improperly collect a discharged debt, which if proved, would entitle the debtor to compensatory damages and possibly further sanctions. The motion to dismiss Counts I and III is denied.

The plaintiff further moves to dismiss Count II because sanctions for violating the discharge injunction must be willful, i.e., the actions must be taken with knowledge the debt was discharged, and willfulness is not alleged. On the contrary, the complaint states that the debtor was contacted by a representative of the plaintiff in January 2010. She told that person the debt was discharged and the person should contact her attorney, but no such contact was made to verify the plaintiff's statement. The "garnishment" began in May 2010. It is therefore pled plausibly that the defendant acted willfully to collect the debt and with knowledge of the debtor's discharge. The motion to dismiss Count II is also denied.

The real issue here is whether the debtor's student loan was indeed discharged. To make that determination, the Court will need facts that were not in any of the pleadings. If it was discharged, the defendant had no right to what it collected, and this Court would have to examine the circumstances to determine whether only a refund is necessary or if additional sanctions are warranted. If it were not discharged, the creditor had a right to collect it, although the procedure used is highly questionable.

A proposed bankruptcy plan becomes effective upon confirmation, *see* 11 U.S.C. §§ 1324, 1325, and will result in a discharge of dischargeable debts provided for by the plan, if the debtor completes the payments the plan requires. *See* 11 U.S.C. § 1328(a). Even with a chapter 13 discharge, certain debts, like student loans in some circumstances, are excepted from that discharge. 11 U.S.C. § 1328(a) (1994). The plaintiff in this case completed required payments to the trustee, and her discharge was issued.

The discharge injunction is created by section 524(a) of the Bankruptcy Code, which states in relevant part:

A discharge in a case under this title ... (2) operates as an injunction against the commencement or continuation of an action, the employment of process, or an act, to collect, recover or offset any such debt as a personal liability of the debtor, whether or not discharge of such debt is waived.

11 U.S.C. § 524(a).

The question raised by the parties is whether or not the University's claim was to be paid by the trustee from plan payments or whether the debtor was to pay the \$1,000 directly. Without question, the trustee did not pay this amount, because of the University's failure to file a proof of claim. Without question, the debt was provided for by the plan, because the specific amount due

the creditor was established. The discharge was issued without any timely objection by the creditor that it did not receive the \$1,000 direct payment it should have been paid pursuant to the plan. But neither the plan, nor the two orders of confirmation, say that completion of the plan will result in the discharge of the student loan. *Cf. United Student Aid Funds, Inc. v. Espinosa*, 130 S.Ct. 1367 (2010) (bankruptcy court's legal error in confirming debtor's plan absent a finding of undue hardship in an adversary proceeding did not render its judgment void). The May 24, 1994, order of confirmation only states the payment of \$1,000 will be in full *settlement* of its allowed claim; it does not say the unpaid debt – either the settlement amount or the amount forgiven by agreement – will be discharged. Furthermore, there was no "allowed claim" because UWM did not file a proof of claim. *See* 11 U.S.C. § 501(a).

Whether or not the obligation was discharged turns on an application of the law in effect in 1994 to the specific facts pertaining to the loans in question – unknown to the Court at this time. Section 523(a)(8) of the Code provided the following:

- (a) A discharge under section ... 1328(b) of this title does not discharge an individual debtor from any debt ...
 - (8) for an educational benefit overpayment or loan made, insured or guaranteed by a governmental unit, or made under any program funded in whole or in part by a governmental unit or nonprofit institution, or for any obligation to repay funds received as an educational benefit, scholarship or stipend, unless
 - (A) such loan, benefit, scholarship, or stipend overpayment first became due more than 7 years (exclusive of any applicable suspension of the repayment period) before the date of the filing of the petition; or (B) excepting such debt from discharge under this paragraph will impose an undue hardship on the debtor and the debtor's dependents

11 U.S.C. § 523(a)(8) (1994). The subject loans were obtained in the early 1980s, so they likely first became due more than seven years before the date of the petition, January 11, 1994. The loans, therefore, would be dischargeable unless there was an "applicable suspension of the

repayment period" for some or all of the loans. Section 523(a)(8)(A) has been interpreted broadly and "refers to an extension of the term of the loan by granting a period of time during which the debtor is not obligated to make payments." *In re Woodcock*, 144 F.3d 1340, 1342 (10th Cir. 1998); *see also In re Gibson*, 184 B.R. 716, 718-19 (E.D. Va. 1995), *aff* d, 86 F.3d 1150 (4th Cir. 1996) (automatic stay under previous bankruptcy filing is an applicable suspension); *Matter of Eckles*, 52 B.R. 433 (E.D. Wis. 1985) (three-month period in which payments were reduced pursuant to forbearance agreement constituted a suspension of the repayment period); *In re Huber*, 169 B.R. 82 (Bankr. W.D.N.Y. 1994) (periods of deferment sought and obtained by debtor because he continued in school were applicable suspensions of repayment period excluded in calculating seven-year period); *In re Cobb*, 196 B.R. 34 (Bankr. E.D. Va. 1996) (if student loan is consolidated, seven-year period begins to run at time of new loan).

Unlike the automatic stay provision in 11 U.S.C. § 362, the discharge injunction provision does not specify any remedy for its violation. Nevertheless, upon a finding of a willful violation of the discharge injunction, courts routinely award damages pursuant to their contempt power under 11 U.S.C. § 105(a). *See, e.g., In re Feagins*, 439 B.R. 165 (Bankr. D. Haw. 2010); *In re Wynne*, 422 B.R. 763 (Bankr. M.D. Fla. 2010). It is not enough to find that a discharge violation has occurred; in order to impose sanctions upon an alleged violator, a court must also conclude that the alleged violator had knowledge of the discharge injunction and intended the actions which violated the injunction. *See In re Weinhold*, 393 B.R. 623, 629 (Bankr. E.D. Wis. 2008). However, before we even get to the violation of the discharge injunction question, the debtor must first prove by clear and convincing evidence that the debt at issue was discharged. *Id.* at 628.

There is not any question that CTI was aware of the debtor's discharge (or at least was informed of such by the plaintiff), and it has not argued otherwise. Moreover, there is no question that CTI intended its collection actions. Nevertheless, to violate the discharge injunction, CTI would have had to have known – or should have known – that the University's claim was included in the debtor's discharge. While this Court holds the dischargeability of this student loan was not determined by whether it was paid directly or by the trustee pursuant to a proof of claim, the plan and confirmation orders are susceptible to differing interpretations. Generally, an ambiguous bankruptcy plan is to be construed against the debtor drafter. See In re Westside Print Works, Inc., 180 B.R. 557, 560 (B.A.P. 9th Cir. 1995). Here, however, the ambiguity is created by the two confirmation orders. Although the trustee probably drafted the first confirmation order, the Order Modifying Confirmed Plan of Arrangement was drafted by debtor's counsel, and any ambiguities created by that order will have to be construed against the debtor. Also, the law regarding discharge of student loans has changed significantly in the intervening years, which might have added to the ambiguity of the situation. Whether the creditor is subject to sanctions for willful and intentional conduct must be decided with this ambiguity as a background.

How the University's claim was to be paid is not clear, especially not now, 15 years after the fact. What is clear, however, is that the debt was provided for by the plan, and the debtor got her discharge. The applicable law provided that a student loan debt was excepted from discharge only if it "first became due more than 7 years (exclusive of any applicable suspension of the repayment period) before the date of the filing of the petition[.]" 11 U.S.C. § 523(a)(8)(A) (1994). Additional evidence is therefore required to make the determination of dischargeability

and possible sanctions, and further proceedings will be scheduled. Based on the reasoning stated above, the defendant's motion to dismiss is denied. A separate order will be entered accordingly.

August 1, 2011

Margaret Dee McGarity
United States Paper Property In

United States Bankruptcy Judge